NSTAR
ELECTRIC
GAS
800 Boylston Street Boston, Massachusetts 02199

July 25, 2005

Mary L. Cottrell, Secretary
Department of Telecommunications and Energy
One South Station, 2nd Floor
Boston, MA 02110

RE: D.T.E. 04-115, Supplemental Comments of NSTAR Electric

Dear Ms. Cottrell:

On June 20, 2005, the Department of Telecommunications and Energy (the "Department") conducted a technical session in the above-referenced proceeding to discuss the following three issues: (1) potential modifications to the procurement schedule for basic-service supply; (2) whether electric distribution companies should be required to enter into long-term contracts for basic service supply to support the development of renewable (generation) technologies; and (3) whether there are other steps that should be taken to further the development of the competitive retail market in Massachusetts. In accordance with the process established by the Hearing Officer, set forth herein are the comments of NSTAR Electric ("NSTAR Electric" or the "Company") regarding the issues discussed at the Department's technical session.

(1) Potential Changes to the Procurement Schedule for Basic Service Supply

As noted by Chairman Afonso in his opening remarks, the Department's overriding policy objective in setting the procurement schedule for basic-service supply has been to balance "price stability and market-based rates" for smaller customers (Tr. at 12). Under the current procurement schedule, electric companies procure electric supply for residential and small commercial and industrial ("C&I") customers in two segments (each 50 percent of the load requirement) on a semiannual basis for a 12-month term (Tr. at 7). Electric supply for larger C&I customers is procured quarterly (id.).

Several commenters, including the electric distribution companies, the Division of Energy Resources (DOER) and Associated Industries of Massachusetts ("AIM") voiced support for the Department's existing procurement schedule. Other commenters suggested: (1) shortening contract terms and/or re-setting prices for residential and small C&I customers on a monthly or quarterly basis rather than six-month basis; (2) establishing an annual price for residential and small C&I customers, or (3) instituting a "laddered approach" involving the procurement of a bundle of contracts for varied terms and amounts.

The proponents of shortening contract terms and/or resetting prices for residential and small C&I customers state that the benefit will be that competitive retail marketers will be in a better position to offer "long-term fixed prices" or other pricing options to "taking volatility out of a basic-service rate" (Tr. at 78). Conversely, setting a longer-term price (i.e., an annual price) could provide a retail marketer with the opportunity to offer a lower basic-service rate (see Tr. at 78-81).

However, from NSTAR Electric's perspective, neither alternative offers a superior approach to the

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Department's existing base-service procurement strategy. Moving to a monthly or quarterly pricing approach for residential and small C&I customers is problematic because a substantial level of price volatility would be introduced to these customer classes without a coincident increase in the competitive options available to them. For example, most, if not all, of the suppliers commenting at the technical session noted that bad-debt risk and acquisition costs are a substantial barrier to the offering of services to customers in these rate classes. Therefore, it is likely that, even with more frequent price changes reflecting market prices and increasing the opportunity for marketers to offer price-management products, customers in these rate classes would not experience a measurable change in the competitive options available to them. As a result, a change in the existing procurement and pricing approach would have only the result of leaving these customers subject to the volatility of the marketplace. In addition, a shorter term pricing increment (i.e., monthly) is likely to lead to a high level of customer confusion for those taking basic service.

Conversely, the benefit of establishing a longer-term (annual) price would be that the marketer may be able to offer a lower price than that fixed at the start of the annual period. However, there is also the potential that this approach would create a barrier to competition where prices are rising in the market (Tr. at 102). In addition, an annual price has more potential to vary from market prices available throughout the year and more potential to result in significant price changes for customers at the end of the term. Neither result is consistent with the Department's overriding policy objectives.

Lastly, several comments were offered on the pros and cons of a more "laddered approach" involving a portfolio of shorter and longer term contracts, as advanced by the Attorney General (Tr. at 43). Based on the comments offered at the proceeding, a more laddered approach would not be advisable because (1) it involves the use of relatively long term contracts where there is less liquidity in the market (Tr. at 68, 135, 158); (2) longer-term contracts are likely to produce higher costs to customers because of the risk premium involved in longer term contracts (Tr. at 68); and (3) the use of multiple contract solicitations and contract terms would tend to "mask" market prices for power (Tr. at 67). Thus, the laddered approach would tend to introduce more complexity, while impeding the presentation of a clear price signal to customers and competitive suppliers attempting to market to those customers. Although it may result in more price stability for customers, the balance between sending a market-based price signal and achieving price stability would not be maintained.[1]

Accordingly, as emphasized by NSTAR Electric and other participants in this proceeding, the Department's existing procurement approach strikes the appropriate balance in terms of establishing a framework for a competitive market and setting a price that is both "market reflective" and affording a level of protection from price volatility.

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1 As noted at the technical session, "the clearer the price signal that you send to customers about the real cost of electricity, the better the market works, the more the competitive the market will be able to develop product offerings, price offerings to customers that fit their needs (Tr. at 222-223)." As the Company understands it, the Department is weighing whether the volatility of the market for smaller customers without full opportunities in the marketplace could be tempered through a change in procurement practices. The current procurement process achieves this goal, where the laddered approach would have a greater tendency to obscure the market price.

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(2) Long-Term Contracts to Support Renewable Technologies

Several commenters suggested that it would be beneficial to require electric distribution companies to enter into long-term contracts for renewable power as part of the basic-service procurement (Tr. at 133, 156, 158). NSTAR Electric continues to believe that there are fundamental policy issues involved in the determination of this issue, which are not appropriate for resolution without comprehensive investigation and consideration in a separate proceeding focused specifically on the benefits and costs that would be visited upon customers.

(3) Furthering the Development of Retail Competition in Massachusetts

The Department has repeatedly stated that its role in carrying out the legislative mandate embodied in the Electric Restructuring Act of 1997, is "to put in place the structural conditions necessary for an efficient competitive process" and "not to guarantee the success of entrants" to the market. See, Gas Unbundling, D.T.E. 98-32-B at 30 (1999). With that in mind, initiatives suggested at the technical session to further the competitiveness of the Massachusetts retail market for electricity included: (1) changing the pricing term; (2) lowering acquisitions costs by allowing customers who are initiating electric service with a distribution company to "opt-in" to supplier service; (3) alleviating bad-debt risk associated with customers transitioning from basic service to supplier service through the "purchase" of supplier receivables.

NSTAR Electric does not support an approach involving the "purchase of receivables" or incurring costs on behalf of customers to shoulder the "bad-debt risk" of competitive suppliers. As noted by supporters of this approach, proposals involving the alleviation of bad-debt risk for competitive suppliers require a "socialization of the bad-debt cost" as a way of "jump-starting" or "promoting" the development of the retail market for smaller customers (Tr. at 244, 264). The Department has a long history of rejecting notions for "jump-starting" the competitive market by increasing costs to customers who remain on basic service. See, e.g., Pricing and Procurement of Default Service, D.T.E. 99-60, at 11 (2000). It is especially notable that a "purchase-of-receivables" program would need "rules which would prevent supplier cherry-picking" (Tr. at 261) and that it would be difficult to end this practice in the future (Tr. at 238). These elements are notable because, in fact, competing suppliers will operate as competitive entities, meaning that they will look for ways to use this program to their benefit in order to compete successfully in the retail market and will become reliant on these programs in terms of factoring costs. NSTAR Electric fully supports the Department's efforts to further the development of a competitive retail market in Massachusetts. To this end, NSTAR supports the suggestion that customers initiating service receive information on how to access competitive supply. As a customer-service organization, however, NSTAR Electric is not in favor of instituting programs that will increase costs for customers remaining on basic service. Nor does NSTAR Electric believe it is in the long-term interests of customers to "promote" competition through the implementation of "jump-start" mechanisms that are designed to ensure the ability of competitors to compete rather than to result in long-term benefits for all customers, including those who are unwilling or unable to participate in the competitive market. As a basic principle, the cost of basic service should not include "artificial" costs that are generated by customers other than those who will be responsible for payment. As noted by the Department:

> Competition is the means to an end -- that end being maximizing consumer welfare. Maximizing consumer welfare means minimizing long-term costs to consumers while maintaining the safety

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> and reliability of electric service. If consumer welfare is maximized with very few customers switching to competitive suppliers, it is not a policy failure, as long as there is free choice and there are no artificial impediments for either suppliers or consumers.

Provision of Default Service, D.T.E. 02-40-B at 6 (2003); D.T.E. 99-60-A at 11. Therefore, the Department should not implement an approach in this case that will increase costs to customers in order to achieve a greater level of customer switching.

(4) Conclusion

NSTAR Electric appreciates the opportunity to comment on the issues raised at the technical session conducted by the Department in this proceeding on June 20, 2005. As stated by AIM at the technical session, the "success in restructuring to date in this state has been the result of extraordinary patience." Tr. at 112. In that regard, the Department has judiciously avoided the "quick fixes" undertaken in other jurisdictions that may shift large numbers of smaller customers over to competitive suppliers, but may also leave the broad base of customers in an environment where they are subject to higher prices, increased price volatility and customer confusion. The Department's efforts have been measured, well considered and successful in balancing competing policy objectives. NSTAR Electric supports continued efforts using this approach.

In addition, given that some of the proposals and issued raised at the technical session were not discussed in the initial round of written comments in this proceeding, NSTAR Electric would appreciate the opportunity to submit reply comments on this new round of discussion and supplemental comments.

Sincerely,

James G. Daly

James Daly
Director, Electric and Gas Energy Supply

cc: Jeanne Voveris, Hearing Officer
Service List, D.T.E. 04-115